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IN THE

Supreme Court of the United States

October Term, 1970
No. 71-118

MASSILLON-CLEVELAND-AKRON SIGN CO.,

Petitioner,

vs.

GOLDEN STATE ADVERTISING CO., INC.; ALBERT A. GOLD; and McCOY-GOLD MERCHANDISING, INC.,

Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

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GOLDEN STATE ADVERTISING CO., INC.; ALBERT A. GOLD; and McCOY-GOLD MERCHANDISING, INC.,
Respondents.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit.

The petitioner Massillon-Cleveland-Akron Sign Co. respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Ninth Circuit entered in this proceeding on June 8, 1971.

Opinions Below.

The judgment and opinion of the Court of Appeals, not yet reported, appears in the Appendix hereto. The Order of the United States District Court for the Central District of California, also unreported, from which the appeal below was taken, similarly appears in the Appendix as does the Settlement Agreement upon which this action is based.

Jurisdiction.

The Court of Appeals decision was, as stated, entered on June 8, 1971 and this petition was filed within ninety (90) days of that date. This Court's jurisdiction is invoked under 28 U.S.C. 1254(1).

Questions Presented.

1. May a party threatened with suit for infringement of an issued patent, who, upon advice of patent counsel, settles and avoids such suit by expressly acknowledging validity of such patent, admitting infringement thereof, and abandoning his right to adjudicate the validity thereof; thereafter repudiate those commitments and judicially attack such validity?

2. Is a covenant by an admitted infringer not to contest validity of a patent contained in an agreement finally and completely settling threatened litigation of such patent, void and unenforceable on its face despite the fact that no license or other continuing right to operate under the patent is given to such infringer in consideration for such covenant?

3. Should this Court's ruling in *Lear, Inc. v. Adkins*, 395 U.S. 653 be applied retroactively to reopen all prior agreements entered into in settlement of threatened patent litigation so as to render void and unenforceable all covenants not to contest validity contained in such agreements?

Statutory Provision Involved.

United States Code, Title 35

"§ 282. Presumption of validity; . . .

A patent shall be presumed valid . . . The burden of establishing invalidity of a patent or any claim thereof shall rest on the party asserting it."

Statement of the Case.

Original federal jurisdiction of this action in the United States district court was predicated on diversity of citizenship. United States Code, Title 28, Sec. 1332.

Petitioner, Massillon-Cleveland-Akron Sign Co. (MCA), is the owner of Letters Patent No. 2,764,830 for "Articulated Banner Unit Construction." Respondents are Golden State Advertising Co., Inc. (Golden State), Albert A. Gold, sole stockholder and President of Golden State, and McCoy-Gold Merchandising, Inc. (McCoy-Gold), a corporation in which Golden State owns a fifty percent interest. McCoy-Gold acts as a sales representative for Golden State.

MCA acquired its patent from the inventor, Edward Frey and in 1962, charged Golden State, Gold, and others not involved in this litigation, with infringement, promising prompt legal action if infringement did not immediately cease.

Expressing an intent to settle and avoid such action, the parties, on July 23, 1962, entered into a written Settlement Agreement (Appendix pp. 13-16). As recited therein, Golden State and Gold, upon advice of patent counsel, acknowledged the validity of the patent, admitted infringement, and covenanted to refrain from further infringement and from directly or indirectly contesting or questioning the validity of the patent. MCA was paid liquidated damages but by express provision in the agreement, no license was given.

In 1964, MCA charged Golden State and Gold with again infringing the patent in breach of the 1962 Settlement Agreement. After representations were made to it, MCA concluded that the 1964 infringement was *de minimis* and not deliberate. When Golden State and

Gold informally expressed an intent to avoid further infringement, MCA elected not to pursue the matter further at that time.

In 1968, it was determined that respondents again were infringing the patent in violation of the Settlement Agreement. MCA therefore brought the present diversity action against respondents and one Monahan, an employee of Golden State, (not a respondent here) alleging in an amended complaint, (1) that Golden State and Gold had breached the Settlement Agreement by infringing the patent and (2) that Gold, McCoy-Gold and Monahan conspired to, and did induce Golden State and Gold to breach the same. An accounting and punitive damages were sought.

In May 1969 McCoy-Gold's affirmative defenses and counterclaim alleging invalidity of the patent were, upon motion of MCA, struck and dismissed by the district court. This on the ground that the action is not one for infringement of a patent, raising issues as to the validity of the patent, but is an action for breach of the Settlement Agreement.

Thereafter, in March 1970, respondents moved the district court to reconsider and vacate its above order of dismissal. They did so on the ground that, under the reasoning of the intervening decision, in June 1969, in *Lear, Inc. v. Adkins,* 395 U.S. 653, defendants were entitled to show a failure of consideration for the Settlement Agreement because the patent might be shown to be invalid. MCA opposed the motion.

In April 1970, the district court entered an order (Appendix pp. 10-12) (certified for interlocutory appeal) denying the motion to vacate the order of May 1969. All defendants in the district court except Monahan[1] appealed from the order denying the motion.

The Court of Appeals reversed and remanded holding that, under the rationale of *Lear,* the covenant not to contest validity of petitioner's patent was "void and unenforceable" and that despite the previous admission of validity and infringement, none of the respondents is precluded from challenging the validity of the patent.

The Court of Appeals further held that the recognized policy favoring settlement of disputes "must give way to the policy favoring free competition in ideas not meriting patent protection."

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[1]In a prior infringement action on the same patent petitioner had obtained a consent judgment declaring, *inter alia,* the patent valid as between petitioner and Monahan. Thus, it is apparent that Monahan conceded that he is foreclosed by the doctrine of *res judicata* from attacking validity.

REASONS FOR GRANTING THE WRIT.

1. The Decision Below Is in Conflict With the Judgment of This Court as to the Proper Interpretation of Lear v. Adkins.

The June 1969 decision of this Court in *Lear* abrogated the rule of licensee estoppel announced twenty years earlier in *Automatic Radio Manufacturing Co. v. Hazeltine Research, Inc.*, 339 U.S. 827. Following *Lear* numerous efforts have been made in cases having fact matrices differing substantially from that of *Lear*, to reopen attacks on patent validity previously foreclosed by estoppel, waiver, covenant or otherwise. One such case (a suit for royalties under a patent license) reviewed in this Court on certiorari, is *Standard Industries, Inc. v. Tigrett Industries, Inc.*, 397 U.S. 586 (1970) wherein this Court, by equally divided opinion, affirmed the lower court decisions upholding validity and infringement of the patent and refused, despite the intervening decision in *Lear*, to order reopening of the case to permit the defendant licensee, Standard, to challenge the validity of the patent there involved.

The dissenting (and only published) opinion in *Standard Industries* indicates clearly that the primary ground for refusing to apply *Lear* in that case was the fact that Standard, by failing to raise the validity question in the courts below, had *waived* its right to do so.

Mr. Justice Black, dissenting in *Standard Industries*, although apparently agreeing that the right to contest validity could, in appropriate circumstances, be waived, pointedly criticizes the finding of a waiver in that case.

He observed that as the law stood prior to *Lear*, it would have been futile for the defendant-licensee to assert invalidity. *Ergo*, such failure to assert that defense was *not*, in Mr. Justice Black's view, a waiver because it was not "an intentional relinquishment or abandonment of a known right or privilege".

But in the case *sub judice* there was set forth in the Settlement Agreement of 1962, precisely such an intentional abandonment of the known right or privilege of respondents Gold and Golden State, at that time, to contest validity. That is, there was a clear and unequivocal *waiver* of that right. Moreover, the express waiver was made after said respondents had been fully advised by patent counsel who had studied the patent and accused devices and at a time when there was no legal impediment whatsoever to the bringing and maintaining by them of an action to contest validity of the patent.

To elaborate briefly, when Golden State, *et al.*, were initially charged with patent infringement, they thereupon had the right and opportunity, if they chose, to attempt to establish invalidity of the patent by joining issue in the threatened litigation.[2] In any such action they would, of course, bear the burden of establishing

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[2]It is clear from the letter originally charging Golden State, *et al.* with infringement that MCA, the patentee, was ". . . prepared to litigate and to litigate to the finish against the defendant there involved". *Blonder-Tongue Lab., Inc. v. University of Illinois Found.*, ... U.S. ....., 91 S. Ct. 1434 at 1444 (May 3, 1971). But even if MCA did not proceed with the action threatened in 1962, Golden State *et al.* could, of course, have sought a declaration of invalidity via the Declaratory Judgment Act (28 U.S.C. 2201 *et seq.*).

invalidity. If they did not sustain that burden, or chose not to assume it, the presumption of validity (35 U.S.C. 282) would remain.

Golden State, *et al.*, were thus faced with, and free to make, the choice between litigation or finally settling the matter by agreement thus allowing the presumption of validity to stand. With full knowledge of the consequences and uncertainties involved in pursuing either course, and with full advice of patent counsel, Golden State, *et al.*, deliberately chose to waive their right to litigate, and chose instead to enter the Settlement Agreement allowing the presumption of validity to stand.

In *Standard Industries* this Court refused to interpret *Lear* in a manner to reopen the case and permit the defendant-licensee to make an attack on validity, where, by mere inaction, it had waived its right to make such an attack. *A fortiori,* in the case at bench where the waiver was made with full knowledge of the right, by affirmative recitals in a written contract, *Lear* is inapposite and the waiver of contest of validity should stand.

We respectfully submit that the judgment and opinion of the court below which refused to recognize the waiver in this case is in direct conflict with the judgment of this Court in *Standard Industries* wherein *Lear* was *not* held to be applicable to relieve the petitioner in that case from its waiver of the right to contest validity. Such conflict justifies the grant of certiorari to review the judgment below.

2. The Decision Below Is in Conflict With Decisions in Other Circuits and Jurisdictions Which Accord Finality to Agreed Settlements of Patent Controversies Including Provisions Acknowledging Validity.

The law strongly favors agreements in settlement of threatened or pending litigation; according them the conclusive attributes of final judgments.[3]

Relying on the foregoing proposition, petitioner argued in the court below that being part of an agreement in settlement of threatened litigation and thus tantamount to a final judgment, the covenant in issue here should be distinguished from the estoppel sought to be implied from the *Lear* license agreement. This on the ground that there was no litigation threatened or even possible at the time the *Lear* license agreement was entered. Petitioner's argument was rejected by the court below with the statement:

> "We think it unimportant that in our case the covenant is part of a settlement agreement rather than of a typical patent licensing agreement . . . If the recognized policy favoring settlement of disputes might be hindered by our holding on this question, that policy, in our opinion, must give way to the policy favoring free competition in ideas not meriting patent protection." (App. p. 6)

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[3] *Hennessy v. Bacon*, 137 U.S. 78 (1890); *St. Louis Mining and Milling Co. v. Montana Min. Co.*, 171 U.S. 650 (1898); *Williams v. First National Bank*, 216 U.S. 582 (1910); *Clark v. Barlow, et al.*, 122 F. 2d 337 (D.C. Cir. 1941) cert. den. 314 U.S. 675 (1941); *J. Kahn & Co. v. Clark*, 178 F. 2d 111 (5th Cir. 1949); *A. D. Juilliard & Co. v. Johnson*, 259 F. 2d 837 (2d Cir. 1958) cert. den. 359 U.S. 942 (1959); *Levy Trust v. C.I.R.*, 341 F. 2d 93 (5th Cir. 1965); *Cia. Avon Venezolana De Navegacion v. Harris*, 374 F. 2d 33 (5th Cir. 1967); *Potter v. Pacific Coast Lumber Co.*, 37 Cal. 2d 592 at 602 (1951); *Central Basin Municipal Water District v. Fossette*, 235 Cal. App. 2d 689 (1965); *County of Los Angeles v. Law Building Corp.*, 254 Cal. App. 2d 848 (1967).

The above quoted view of the law as seen by the court below is in stark contrast to the rule in other circuits under fact situations involving settlement agreements terminating or obviating litigation.

The rule to be applied to out-of-court settlement agreements is, we submit, the same as applied in according finality to consent judgments, for example *Crane Boom Life Guard Co., Inc. v. Saf-T-Boom Corp.*, 362 F. 2d 317 (8th Cir. 1966) cert. den. 386 U.S. 908 (1967).

Crane Boom involved a settlement agreement pending trial, pursuant to which a consent decree providing a permanent injunction was issued.

In a subsequent contempt proceeding the accused contemners, Crane Boom and others not parties to the original action, sought relief from the final judgment and to reopen the question of the validity of the patent. It was argued that because of the public interest in striking down invalid patents, and because the judgment in that case merely reflected an agreement between the parties, Crane Boom *et al.* should not be barred by the consent judgment from making a new attack on the patent. The trial court denied relief from the consent judgment and held the parties accused of contempt to be foreclosed from attacking the validity of the patent.

On appeal the Court of Appeals for the Eighth Circuit, after a thorough consideration and discussion of the public interest argument advanced in the trial court, nevertheless, affirmed the trial court's enforcement of the estoppel to contest validity.

It bears emphasis that in reaching the above decision and distinguishing the authorities cited by appellant

Crane Boom, the appellate court observed that an essential element required to give finality to a consent decree of validity, is a clear indication that infringement had occurred and that the parties agree to an adjudication thereof *e.g.* by consenting to an award of damage or an injunction. See 362 F. 2d 317 at 321-322. In other words, where a patent infringement charge is settled by agreement, such settlement is given conclusive effect where it clearly appears that the parties intended to resolve finally and conclusively, the question of prior infringement of the patent in question.

This essential element is clearly present in the Settlement Agreement *sub judice* since the respondents Gold and Golden State not only expressly acknowledged validity, but unequivocally admitted prior infringement and paid damages therefor.

It is clear, we submit, that no basis exists for distinguishing the present Settlement Agreement arrived at prior to suit from those like in *Crane Boom* which are entered after suit is filed. A consent judgment does not involve a judicial determination of fact but merely records the agreement of the parties. See *e.g.* Rule 68, Federal Rules of Civil Procedure under which the *Clerk* may enter judgment pursuant to an offer and acceptance by the parties.

The rule of *Crane Boom*—according full *res judicata* effect to consent judgments in patent cases entered pursuant to settlement agreements—has also been followed in several other circuits[4] and the principles un-

[4]First Circuit (*Gloucester Isinglass & Glue Co. v. Le Page*, 30 Fed. 370 (1887)) Second Circuit (*Hopp Press, Inc. v. Jos. Freeman and Co.*, 323 F. 2d 636 (1963)); Fifth Circuit (*Dow Chemical Co. v. Chemical Cleaning, Inc.*, 434 F. 2d 1212 (1970) cert. den. ..... U.S. ....., 91 S. Ct. 1621 (1971)

derlying the rule were applied, correctly we submit, by the district court in the case at bench.

Nothing in *Lear* requires or even suggests a change in the above rule. The *Lear* facts are significantly different from those in *Crane Boom* and other consent judgment cases where prior infringement of the patent is admitted. In *Dow Chemical v. Chemical Cleaning, supra,* 434 F. 2d 1212 the patent there involved had been declared valid and infringed in a consent decree[5] and pursuant to agreement between the parties an injunction issued. Thereafter, in a contempt proceeding defendant unsuccessfully sought to reopen the validity question on the specific grounds that the intervening decision in *Lear* had changed the law. Certiorari was denied by this Court.

Since Lear did not and could not involve the final settlement of a pre-existing infringement controversy (the Lear-Adkins license agreement antedated the patent by several years) the element essential to the estoppel applied in *Crane Boom* and as we have shown, applicable here, was *not* present in *Lear.*

Furthermore, there was nothing in the facts underlying the agreement in *Lear* providing a basis for implying a deliberate concession by Lear of either validity or infringement. Quite the contrary; the question of validity was expressly left open in the license agreement in that case.

(Facts and attempted application of *Lear* rule set forth in petition for certiorari, *Chemical Cleaning v. Dow Chemical.* No. 1478 Oct. Term 1970); Sixth Circuit (*Warner v. Tennessee Products Corp.,* 57 F. 2d 642 (1932) cert. den. 287 U.S. 632 (1932)); and Seventh Circuit (*Brunswick Corp. v. Chrysler Corp.,* 408 F. 2d 335 (1969).

[5]*See Chemical Cleaning Co. v. Dow Chemical Co.* petition for writ of certiorari No. 1478 Oct. Term 1970, page 5.

The court below sought to justify its rejection of petitioner's foreclosure-by-agreed-settlement argument by reference to a license case, *Edward Katzinger Co. v. Chicago Metallic Mfg. Co.*, 329 U.S. 394 (1947), pointing out correctly that the license there involved was given after a charge of infringement had been made. However, the gravamen of *Katzinger* was the illegality of the unseverable price fixing provisions in the license itself which made *all* provisions thereof unenforceable. Furthermore, there is no indication in the report of that case, that the license agreement conceded infringement or purported to be a final, or any, settlement of threatened litigation.

The taking of a license by one charged with infringement is not, in and of itself, necessarily an admission of infringement or validity of the patent. It is more consistent with an intent on the part of the licensee to hold open and defer the resolution of the infringement and validity questions, paying continuing royalties as the price for such deferment. As noted by this Court in *Blonder-Tongue Inc. v. University of Illinois Foundation*, ... U.S. ...., 91 S. Ct. 1434 (May 3, 1971):

> "*Lear* permits an accused infringer to accept a license, *pay royalties for a time*, and cease paying when financially able to litigate validity, secure in the knowledge that invalidity may be urged when the patentee-licensor sues for unpaid royalties." 91 S. Ct. 1434 at 1451 (emphasis added).

But this is not the same as permitting one to effect what purports to be a final settlement of threatened litigation by making an unequivocal admission of infringement and concession of validity and yet be secret-

ly secure in the knowledge that he may thereafter repudiate such admission and concession at will. *Lear* certainly does not purport to condone such blatant dishonesty.

Summing up on this point, petitioner submits that the court below, in failing to distinguish between the final Settlement Agreement *sub judice* and the prepatent license agreement in *Lear,* has created a wide conflict with the rule in cases such as *Crane-Boom, supra,* 364 F. 2d 317 in the Eighth Circuit and *Dow Chemical, supra,* 434 F. 2d 1212 in the Fifth Circuit which, while recognizing the public interest in eliminating invalid patents, nevertheless give conclusive effect to agreements which are clearly intended as final settlements of patent litigation.

It is further submitted that the salutory principles stated in *Lear* do not warrant, much less require, the holding of the court below. Therefore, review by this Court is required to resolve the above noted conflict.

3. The Holding of the Court Below Represents a Substantial Departure From Prior Treatment of Out-of-Court Settlement Agreements, Raises Important and Recurring Problems in That Regard, and Would Foster a Significant Increase in Pointless Litigation.

The record in this case shows that the agreement in question was the result of a good-faith effort by petitioner to effect final settlement of a patent controversy without the necessity of trial and the heavy expenses to both parties and extraordinary consumption

of judicial time and effort involved in the trial of patent cases.[6] Prior to such settlement, respondents had a clear opportunity to litigate validity if they chose, and no element of fraud, coercion or other unfairness in reaching the agreement is even suggested. Now, however, some nine years later, the settlement has been substantially frustrated by the holding of the court below that respondent's covenant not to contest validity "is void on its face and unenforceable." Moreover that holding is in such sweeping and all-inclusive terms as to bring every kind of consensual settlement agreement within its reach, including consent judgments. If the rule stated by the court below were to be followed, there would no longer be any substantial incentive for patentees to compromise or settle controversies concerning infringement of their patents—either before or during trial. Under such circumstances virtually every case in which an accusation of infringement was made would have to be litigated, and litigated to the bitter end, however willing the accused infringer might be to admit infringement and agree to desist.

Moreover the defense of a patent infringement action by a defendant who would rather settle than litigate, would reduce the trial of such action to a sham battle unlikely to provide a real test of patent validity.

Such a rule of law is such a violent departure from the long accepted and highly desirable policy of curtailing litigation by encouraging good faith settlement between the parties, that it should not, in petitioner's submission, be adopted as the overriding policy applicable

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[6]The relatively high cost of patent litigation in money and judicial effort is discussed and documented in *Blonder-Tongue, supra*, 91 S. Ct. 1434 at 1445-1447.

to any and all patent settlement agreements heretofore or hereafter entered.

An examination of the patent trial statistics set forth in *Blonder-Tongue* together with a consideration of the obvious fact that many more patent controversies are settled than are litigated, discloses that the adoption of the rule stated by the court below, threatens a very significant increase in litigation of patents.

This court found it necessary in *Blonder-Tongue* to review and restate the law of *res judicata* and collateral estoppel as applicable to the prior practice of re-litigating patents once held invalid. One of the important reasons given for the ruling in *Blonder-Tongue* is the inordinate amount of trial time consumed by patent cases that go to trial (91 S. Ct. 1434 at 1447) and the reduction in this consumption of judicial time and effort to be effected by elimination or at least curtailment of multiple litigation of patents once adjudicated invalid.

In the nature of things it is evident that by substantially eliminating, as the court below would do, the effectiveness of out-of-court settlement, much more patent litigation is likely to be *fostered* than could possibly be eliminated by the strictest application of the *Blonder-Tongue* rule.

We do not seek to deprecate in any way the rule of *Lear* as we understand it and as it was clarified and restated in *Blonder-Tongue*. But we respectfully submit that the rule of *Hennessy v. Bacon* first applied in this Court at least as early as 1890 and consistently followed ever since, is of at least equal stature and dignity and need not and should not be abrogated in patent cases because of its alleged obstruction to the elimination of invalid patents.

Both public policies should be given effect and when accused infringers knowingly enter agreements conceding validity and infringement of the subject patents with the express intent of thereby finally and completely disposing of those questions, the public policy underlying *Lear* does not require, nor indeed would it be served by, nullification of such agreements.

Conclusion.

For the reasons set forth above we urge that a writ of certiorari issue enabling this Court to review and resolve the significant uncertainties and important conflicts inherent in the decision of the court below.

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EXHIBIT A.

Opinion of the Court of Appeals for the Ninth Circuit.

United States Court of Appeals for the Ninth Circuit.

Massillon-Cleveland-Akron Sign Co., a corporation, Appellee, v. Golden State Advertising Co. Inc., a corporation, Albert A. Gold, William Monaghan, and McCoy-Gold Merchandising, Inc., a corporation, Appellants, No. 25,873.

[June 8, 1971].

Appeal from the United States District Court for the Central District of California.

Before: HAMLEY, BROWNING and TRASK, Circuit Judges.

HAMLEY, Circuit Judge:

This is an interlocutory appeal, taken pursuant to 28 U.S.C. § 1292(b), from a district court order striking certain affirmative defenses and a counterclaim asserted by one of the defendants.

The plaintiff and appellee is Massillon-Cleveland-Akron Sign Co. (MCA), which is the owner of Letters Patent No. 2,764,830 for "Articulated Banner Unit Construction." The defendants are Golden State Advertising Co., Inc. (Golden State), Albert A. Gold, sole stockholder and President of Golden State, William Monaghan, an employee of Golden State, and McCoy-Gold Merchandising, Inc. (McCoy-Gold), in which Gold owned a fifty percent interest. McCoy-Gold acts as a sales representative for Golden State.

MCA acquired its patent from the original patentee, Edward Frey. In 1962, MCA charged Golden State, Gold, and others not involved in this litigation, with

infringement of the patent. MCA informed Golden State and Gold that legal action would be taken if they did not cease infringement activities and if they did not account for sales of the infringing items.

This threatened legal action was forestalled when the concerned parties, on July 23, 1962, entered into a written agreement settling the controversy. Under the terms of the agreement, Golden State and Gold acknowledged the validity of the patent and covenanted to refrain from directly or indirectly contesting or questioning the validity of the patent. Golden State and Gold also therein admitted having infringed the patent and covenanted that they would not infringe the patent in the future. As called for in the agreement, Golden State and Gold paid MCA five hundred dollars as liquidated damages.

In 1964, MCA again charged Golden State and Gold with infringing the patent and further asserted they breached the 1962 stttlement agreement. After representations were made to it, MCA concluded that the 1964 infringement was not deliberate and involved sales of only a few units. When Golden State and Gold informally expressed an intent to avoid further infringement, MCA elected not to pursue the matter further at that time.

In 1968, MCA received information leading it to believe that Golden State and Gold again were infringing the patent and had breached the settlement agreement. MCA therefore brought this action against them and others. In its amended complaint, MCA alleged that Golden State and Gold had breached the settlement agreement by infringing the patent. Plaintiff also named, as defendants, McCoy-Gold and Monaghan. MCA alleged that Gold, McCoy-Gold and Monaghan

conspired to and did induce Golden State to breach the settlement agreement. Finally, MCA alleged that McCoy-Gold and Monaghan induced Gold to breach the agreement. MCA sought an accounting and asked for punitive damages.

McCoy-Gold's answer, in part, raised the issues of misuse of the patent and the patent's invalidity by way of affirmative defenses and counterclaim. Upon motion of MCA, the district court, on May 23, 1969, struck these portions of the affirmative defenses and dismissed the counterclaim. It did so on the ground that this is not an action for infringement of a patent, raising issues as to the validity or misuse of the patent, but is an action for breach of the settlement agreement.[1]

Thereafter, on March 6, 1970, all of defendants moved the district court to reconsider and vacate its order of May 23, 1969. They did so on the ground that, under the reasoning of the intervening decision, on June 15, 1969, in *Lear, Inc. v. Adkins,* 395 U.S. 653, defendants were entitled to show a failure of consideration for the settlement agreement because the patent is invalid. MCA opposed the motion. On April 29, 1970, the district court entered an order denying the motion to vacate the order of May 23, 1969. The district court held that *Lear* is distinguishable and does not entitle defendants to question the validity of the patent in this action on the settlement agreement. All defendants then joined in this interlocutory appeal,[2] except Monaghan.

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[1]An appeal from this order was docketed in this court on June 25, 1969, as No. 24,469. This court later dismissed that appeal upon the motion of MCA.

[2]Thus while the order under review specifically dealt only with the answer filed by McCoy-Gold, all defendants feel aggrieved

(This footnote is continued on next page)

Golden State and Gold are charged with breach of a covenant not to infringe MCA's patent, and in our view the single question presented on appeal, with respect to this allegation, is whether, in light of *Lear*, the express covenant, in which Gold and Golden State agreed to refrain from directly or indirectly contesting the validity of MCA's patent, is illegal and unenforceable.

Lear did not specifically deal with the validity of such a covenant. Instead *Lear* concerned itself primarily with a re-examination of the rule, stated in *Automatic Radio Mfg. Co. v. Hazeltine Research, Inc.*, 339 U.S. 827, 836 (1950), that the licensee under a patent license agreement is estopped to challenge the validity of the licensed patent in a suit for royalties due under the contract. The court called attention to stringent limitations which past decisions had placed upon the doctrine of licensee estoppel, noting that this had left the doctrine in an uncertain state. This uncertainty, the court observed, was a product of judicial efforts "to accommodate the competing demands of the common law of contracts and the federal law of patents." 395 U.S. at 668. The Court observed:

> "On the one hand, the law of contracts forbids a purchaser to repudiate his promise simply because he later becomes dissatisfied with the bargain he has made. On the other hand, federal law requires that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent." 395 U.S. at 668 (footnote omitted).

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thereby. While the answering pleadings of the other defendants are not in the record before us, it is recited in the agreed statement that all defendants seek to attack the validity of the patent. We will accordingly assume, as have the parties, that the order under review is adverse to all defendants.

In *Lear,* the Supreme Court concluded that there was no satisfactory intermediate position between these competing demands, and resolved the conflict in favor of the policy behind the federal law. The Court, characterizing *Automatic Radio Mfg. Co., v. Hazeltine Research, Inc., supra,* as "the product of a clouded history," expressly overruled that decision. The Court held that Lear, Inc. must at least be permitted to avoid the payment of all royalties accruing after Adkins obtained his patent, despite an express contractual provision obligating Lear, Inc. to pay royalties until the patent is held invalid, if Lear, Inc. can prove patent invalidity. The Court said:

> "The parties' contract, however, is no more controlling on this issue than is the State's doctrine of estoppel, which is also rooted in contract principles. The decisive question is whether overriding federal policies would be significantly frustrated if licensees could be required to continue to pay royalties during the time they are challenging patent validity in the courts.
>
> . . .
>
> ". . . enforcing this contractual provision would undermine the strong federal policy favoring the full and free use of ideas in the public domain." 395 U.S. at 673-674.

We think the rationale of *Lear* requires us to hold that the covenant of Golden State and Gold, in the settlement agreement of July 23, 1962, not to contest the validity of MCA's patent, is void on its face and unenforceable. It is in just as direct conflict with the "strong federal policy" referred to repeatedly in *Lear,* as was the estoppel doctrine and the specific contractual provision struck down in that decision.

In an earlier Supreme Court case, *Edward Katzinger Co. v. Chicago Metallic Mfg. Co.*, 329 U.S. 394 (1947), the Court dealt specifically with the enforceability of a covenant not to challenge the validity of a patent. The Court held that such a provision "can no more override congressional policy than can an implied estoppel." 329 U.S. at 402. In our case, as in *Katzinger*, the covenant not to contest validity of the patent cannot over-ride federal policy.

We think it unimportant that in our case the covenant is part of a settlement agreement rather than of a typical patent licensing agreement. Were we to recognize such a distinction it would, in practice, be less than workable. The licensing arrangement in *Katzinger*, at 395, arose from a charge of infringement. Similarly, it would be just as easy to couch licensing arrangements in the form of settlement agreements. If the recognized policy favoring settlement of disputes might be hindered by our holding on this question, that policy, in our opinion, must give way to the policy favoring free competition in ideas not meriting patent protection.

The second issue presented on this appeal concerns the right of Gold and McCoy-Gold to assert patent invalidity as a defense to the charge of having induced the breach of a contract not to infringe.

For the most part the parties, in their argument here, have not distinguished the position of defendants charged with inducing the breach from that of the defendants charged with the breach. As we view the matter of their positions are not necessarily the same.

Generally, the focus of the arguments in the district court and here has been on the express covenant by Gold and Golden State not to question the validity of the patent. But under the facts here McCoy-Gold is not

bound by the terms of the agreement. While Gold is not precluded from raising the validity of the patent merely because he covenanted not to do so, this does not foreclose the question of whether he may challenge the patent's validity as a defense to the inducement to breach charge.

If either McCoy-Gold or Gold is to be precluded from challenging the patent's validity, with respect to the inducement to breach charge, it stems from MCA's argument that local law precludes a party, who allegedly induced the breach of a covenant not to infringe, from raising such matters.

Were this an action for infringement and for inducing infringement, without the additional element of the contract, a party who induced others to infringe would be liable as an infringer. 35 U.S.C. § 271 (b). In an action involving infringement, invalidity is an available defense. 35 U.S.C. § 282. Therefore, the question is whether the additional element of the contract serves to preclude the issue of invalidity of the patent.

The law gives the patent holder the benefit of a presumption of the patent's validity, and the holder of a patent need not exact from others a promise not to infringe, for the law gives the holder a remedy for conduct that infringes. But the remedy, designed to afford no more protection than public policy allows, depends in part upon the validity of the patent.

If a patent holder can exact from another a promise not to infringe, and thereby recover from one inducing the breach of that promise, in the absence of a valid patent, the patent holder is afforded more protection than the patent laws allow. The patent holder acquires this additional protection "merely because he [MCA

here] chose one remedy [inducement to breach a contract not to infringe] rather than another [inducement to infringe] on the same substantive issue." *Katzinger*, at 399-400. Federal policy favoring free competition in ideas not meriting patent protection cannot be so easily subverted.

In addition, the equities of the patent holder do not weigh heavily when balanced against the "important public interest in permitting full and free competition in the use of ideas which are in reality in the public domain." *Lear*, at 670. Like the licensee, the one inducing the breach may be the only party with the economic incentive to challenge the validity of the patent.

Without the inducement, the contract and the patent probably would have been honored. Thus the act of inducing the breach, perhaps even more so than the act of breaching the contract, exemplifies a willingness to shoulder the burden of vindicating the public interest. To hold a party liable for damages for inducing the breach, in the absence of a valid patent, is as inimical to the public interest as the now defunct principle of licensee estoppel.

Needless to say, one inducing the breach of such a contract, as well as one inducing the infringement of a patent, runs the risk that he may not be able to establish patent invalidity. Nothing said herein is intended to commend one who induces the infringement of a valid patent, or who induces the breach of a contract not to infringe a valid patent. But we are of the opinion that a valid patent is a prerequisite to recovery for inducing the breach of a contract not to infringe, as well as a prerequisite to recovery for the breach itself.

A third question lurks in this appeal, namely defendants' contention that the district court erred in striking from McCoy-Gold's answer its defense that MCA has misused the patent by exacting a promise from Gold and Golden State not to contest the patent's validity.[3]

We say the question "lurks" in the appeal because, while defendants refer to the matter of misuse they do not deal with the specific question of whether one alleged to have induced a breach of a settlement agreement may assert such a defense. Nor has MCA discussed the point in its brief on appeal. For this reason, and because such a defense presumably would be reached only in the event MCA prevails on both patent validity and patent infringement, we decline to render a definitive decision on this interlocutory appeal as to whether such a defense is available to any of the defendants.

Reserving that question, however, we think defendants should be permitted to plead that defense, if they wish, so that the relevant facts may be developed in the event the issue of patent misuse is reached in the further district court proceedings. This will enable the parties to present the question on a second appeal, if this becomes necessary, in a concrete factual setting, and to present an adequate legal discussion of the matter.

Reversed and remanded for further proceedings consistent with this opinion.

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[3]Since we do not have the answers filed by the other defendants, and the matter is not dealt with in the agreed statement of facts, we do not know whether any defendant other than McCoy-Gold asserted this defense.

EXHIBIT B.

Order Re

(a) Plaintiff's Objections to Interrogatories;

(b) Plaintiff's Motion for Protective Order; and

(c) Defendants' Motion to Rescind Prior Order.

In the United States District Court,[1] Central District of California.

Filed April 29, 1970 Clerk, U.S. District Court, Central District of California.

Massillon-Cleveland-Akron Sign Co., a corporation, Plaintiff, vs. Golden State Advertising Co., Inc., a corporation, Albert A. Gold, William Monaghan, and McCoy-Gold Merchandising, Inc., a corporation, Defendants. Civil Action No. 68-1696-CC.

Massillon-Cleveland-Akron Sign Co., a corporation, Plaintiff, vs. Golden State Advertising Co., Inc., a corporation, Albert A. Gold, Defendants. Civil Action No. 69-483 CC.

On April 20, 1970, the following matters came on regularly for hearing before the Honorable Charles H. Carr in the above-entitled court:

(a) Plaintiff's Objections to Defendants' Second Interrogatories No. 3(a) through (j), 4 and 5 (others of said second interrogatories having been withdrawn pursuant to agreement between counsel);

(b) Plaintiff's motion for a protective order re discovery; and

(c) Defendants' motion for an order rescinding the Court's prior ruling herein that the valid-

[1]A stenographic error in designation of the District Court has been corrected by petitioner.

ity of Plaintiff's patent is not an issue herein, said motion being predicated upon the decision of the United States Supreme Court in *Lear vs. Adkins,* 395 U.S. 653 which was rendered subsequent to said prior ruling of this Court.

At said hearing, it was agreed between respective counsel that the Court's ruling with respect to Item (c) above would be dispositive of Items (a) and (b), i.e., that if the Court granted Defendants' motion, Plaintiff's objections (a) should be overruled and its motion, (b) denied and conversely if Defendants' motion (c) were denied, Plaintiff's objections (a) should be sustained and its motion (b) granted. Accordingly, argument at said hearing was confined to Item (c).

Having duly considered the foregoing and the arguments written and oral presented by the respective parties, and being fully advised in the premises, it is

HEREBY ORDERED as follows:

1. Defendants' motion, Item (c) above, is denied, the Court being of the view that the agreement which is the subject of the present action being a compromise and settlement of threatened litigation[2] and not involving a license, is distinguishable from the *Lear v. Adkins* case which involved a license agreement entered into prior to the issue of the licensed patent.

2. Plaintiff's objections, Item (a) above, are sustained; and

3. Plaintiff's motion, Item (b) above, is granted and pending further order of this Court,

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[2]For the convenience of the Court, petitioner has included in this appendix as Exhibit C immediately following this order, a copy of the Settlement Agreement.

Defendants and all of them shall refrain from inquiring of Plaintiff or any witness by written or oral interrogatory or otherwise under the Federal Rules of Civil Procedure as to any matter relating solely to the validity of the Frey patent (U.S. Patent No. 2,764,830). Plaintiff's request for attorneys' fees attendant to the bringing of this motion is denied.

At the request of counsel for Defendants, it is hereby certified, pursuant to the provisions of 28 U.S.C. 1292 (b) that the Court is of the opinion that the above order involves a controlling question of law as to which there is substantial ground for difference of opinion, and that an immediate appeal from said order may materially advance the ultimate determination of this litigation.

Dated this 29 day of April, 1970.

Charles H. Carr
United States District Judge

Approved As To Form this 27th day of April, 1970.
Warren T. Jessup /s/
Attorneys for Defendants

EXHIBIT C.

Agreement.

THIS AGREEMENT, made and entered into as of this 23rd day of July 1962, by and between MASSILLON-CLEVELAND-AKRON SIGN CO., of Massillon, Ohio (hereinafter called M-C-A) as first party, and GOLDEN STATE ADVERTISING CO., INC. (hereinafter called GOLDEN STATE), ALBERT A. GOLD (hereinafter called GOLD), GANGI STUDIOS, INC. (hereinafter called GANGI STUDIOS), and PAUL GANGI (hereinafter called GANGI), jointly and severally as second parties, said second parties being referred to hereinafter collectively as "MANUFACTURERS",

WITNESSETH:

WHEREAS, M-C-A is the present owner by assignment of the entire right, title and interest in United States Letters Patent No. 2,764,830, issued October 2, 1956, on an invention of Edward Frey for ARTICULATED BANNER UNIT CONSTRUCTION, including the right to recover for all past infringement thereof, said United States Letters Patent being hereinafter referred to as "THE SUBJECT PATENT"; and

WHEREAS, M-C-A has heretofore charged MANUFACTURERS with infringement of THE SUBJECT PATENT and has requested that MANUFACTURERS cease and desist from said infringement and account to M-C-A therefor; and

WHEREAS, patent counsel for MANUFACTURERS has investigated and studied THE SUBJECT PATENT and the devices alleged by M-C-A to infringe the same, and has fully advised MANUFACTURERS in the premises; and

WHEREAS, all parties hereto desire to settle this matter without trial and without the cost of detail accounting procedures;

NOW, THEREFORE, in consideration of the foregoing, the following mutual covenants and conditions, the hereinafter described payment to M-C-A, and other good and valuable consideration, the parties agree as follows:

1. ACKNOWLEDGEMENT OF VALIDITY OF THE SUBJECT PATENT.

MANUFACTURERS jointly and each for himself acknowledge the validity of THE SUBJECT PATENT and M-C-A's ownership thereof, and further covenant jointly and each for himself that each will refrain from directly or indirectly contesting or questioning or being a party to the contesting or questioning of the validity of THE SUBJECT PATENT.

2. ADMISSION OF INFRINGEMENT.

MANUFACTURERS admit that within the year last past they have, in cooperation, concert and participation with each other, manufactured and sold in the Southern Judicial District of California a substantial number of articulated banner units which infringe THE SUBJECT PATENT.

3. DAMAGES.

MANUFACTURERS represent and warrant that the only banner units of the type and construction which infringe THE SUBJECT PATENT which they have ever manufactured or sold comprise two orders, one sold to the Pepsi-Cola Corporation and the other sold to the Wilshire Oil Company. Recognizing the difficulty and cost of arriving at an exact accounting of dam-

ages resulting from such sales, the parties have agreed upon, and MANUFACTURERS tender herewith the sum of Five Hundred Dollars ($500.00) as fair liquidated damages due M-C-A by reason of MANUFACTURERS' aforementioned infringement.

4. COVENANT NOT TO INFRINGE.

MANUFACTURERS jointly and each for himself and for the officers, directors, and managing agents of GOLDEN STATE and GANGI STUDIOS covenant and agree that they will not directly or contributorily infringe or induce anyone else to infringe THE SUBJECT PATENT.

5. RELEASE.

Subject to said payment of Five Hundred Dollars ($500.00) and to the due performance of all covenants by MANUFACTURERS contained herein and subject to the correctness of the representation and warranty by MANUFACTURERS contained in Paragraph 3 hereof, M-C-A hereby releases MANUFACTURERS and each of them from all further claims for damages by reason of said infringement by MANUFACTURERS up until the date hereof but not hereafter, and the aforesaid banner units sold to Pepsi-Cola Corporation and Wilshire Oil Company shall from the date hereof be deemed to have been manufactured and sold under license from M-C-A, PROVIDED further, however, that nothing contained herein shall be deemed a license or consent to any manufacture, sale or delivery of banner units or parts after the date hereof.

6. ENTIRE UNDERSTANDING.

This agreement constitutes the entire understanding between the parties relative to THE SUBJECT PATENT and MANUFACTURERS' infringement thereof.

7. SUCCESSION.

This agreement shall be binding upon and inure to the benefit of the successors and assigns of the parties hereto.

8. PARAGRAPH HEADINGS.

The paragraph headings herein are for guidance only and are not to be construed as modifying or limiting any provision hereof.

IN WITNESS WHEREOF, the parties have each and all executed this agreement as of the day and year first above written.

MASSILLON-CLEVELAND-AKRON SIGN CO.
By /s/ Sam Mollett III, Exec. V. P.

GOLDEN STATE ADVERTISING CO., INC.
/s/ Albert Gold

GANGI STUDIOS, INC.
By /s/ Gangi Studios, Inc.
/s/ Albert A. Gold
Albert A. Gold
/s/ Paul Gangi
Paul Gangi